

Canada Revenue Agency's Demand For Oral Interviews of Taxpayer's Employees Refused by Court

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In this article, the author discusses the Canadian Federal Court's recent judgment in *Cameco*, which limited the Canada Revenue Agency's power to demand taxpayer information in audits.

A recent decision of the Federal Court of Canada provides a reassuring illustration of the role of the courts in preventing tax authorities from overreaching on the use of their considerable powers. Any self-assessing tax system necessarily requires that tax authorities have the practical ability to audit and (where appropriate) challenge the positions taken by taxpayers, which in turn necessitates the power to obtain taxpayer information. However, there must be reasonable limitations on the scope of that power, and the Federal Court's judgment of August 10 in *Minister of National Revenue v. Cameco Corporation*, 2017 FC 763, demonstrates that the courts will enforce those limitations when necessary to preserve fairness.

Facts

Cameco is one of the world's largest uranium producers. Its uranium sales to foreign subsidiaries during several years are the subject of complex and lengthy transfer pricing litigation currently before the Tax Court of Canada involving hundreds of millions of dollars. The litigation resulting in the August 10 decision involves the audit by the Canada Revenue Agency

of the taxpayer's 2010, 2011, and 2012 tax years (which are not before the Tax Court at this stage) on essentially the same issue. For each of those years, Cameco provided the CRA with full access to its books, records, and documents.

However, the CRA demanded oral interviews of 25 named employees of the taxpayer and its subsidiaries (and possibly more, should the CRA so insist). Cameco refused this demand, and the CRA went before the Federal Court seeking a compliance order, resulting in the August 10 decision. Cameco's submissions to the court alleged that the CRA's demands were nonproportional, vague, overbroad, and prejudicial to the litigation already before the Tax Court on the earlier years. The Federal Court found in favor of the taxpayer on the basis that the compliance order sought by the CRA "does not meet the principle of proportionality" and so did not address Cameco's other arguments.

The Court's Decision

The Federal Court expressed agreement with the CRA's "general interpretation of the law" in the abstract but not with its application of that law to the unusual facts of this case. The court noted the similarities in the very "wide" interpretation of the relevant statutory provision (subsection 231.1(1) of the Income Tax Act (Canada)) put forth by the CRA both in this case and the recent case of *BP Canada Energy Co. v. Minister of National Revenue*, 2017 FCA 61, in which the Federal Court of Appeal refused to grant the CRA a compliance order compelling the taxpayer to turn over its tax accrual working papers.¹ In that earlier case, the

¹For prior coverage, see Steve Suarez, "Canadian Appeals Court Denies CRA Demand for Taxpayer's UTP List," *Tax Notes Int'l*, Apr. 24, 2017, p. 288.

Federal Court of Appeal found that the CRA's powers under that provision were certainly broad but not unlimited when considered in context, and noted that subsection 231.1(1) did not entitle the CRA to compel taxpayers to "reveal their soft spots" or obtain "general and unrestricted access to those parts of BP Canada's tax reserve papers which reveal its uncertain tax provisions."

Similarly, in *Cameco* the Federal Court concluded that subsection 231.1(1) "is not so wide as to compel an indeterminate number of people for oral interviews" or "provide the Minister with an unlimited right to conduct oral interviews of Cameco employees." The relevant provisions should be interpreted on the basis that Parliament could not have intended for there to be no restraint on how the Minister of National Revenue questions employees of a corporation, and in *Cameco's* case there were several "unique and compelling facts" mitigating against allowing the CRA's demand, including:

- the fact that the issue at stake (transfer pricing) spanned a number of different years;
- the fact that Cameco otherwise fully complied with all previous CRA requests;
- the number of interviews being demanded (and the compromise offered by Cameco); and
- the fact that essentially the same subject matter was already the subject of litigation before the Tax Court.

The fact that the same issues were already in the process of being litigated for other years was clearly an important consideration in the Federal Court's decision. The court noted in paragraph 44 of its decision that granting the CRA its order for oral examinations "imposes a much broader form of examination for discovery than allowed before the Tax Court of Canada without any of the procedural safeguards." Specifically, at a formal examination for discovery in tax litigation, Cameco would be entitled to choose its own representative to be examined, and various Tax Court rules on the scope of the examination, the permitted use of the results, and the consequences of refusing to answer would apply. Indeed, the court found that since the existing Tax Court litigation would likely address (and resolve) most of the issues that would be the subject of the oral interviews, granting the compliance order would

not meet the principle of proportionality and could in fact prejudice those existing proceedings. The court determined that written questions rather than oral interviews would be appropriate.

Analysis

This case is interesting on numerous levels. First of all, it demonstrates how assertively the CRA is willing to explore the limits of its statutory powers to obtain information from taxpayers. Similar to the aggressive pursuit of tax accrual working papers in the *BP Canada* case, the number of interviews sought from Cameco employees is extraordinary, particularly in the context of the ongoing litigation dealing with the same subject matter in earlier years.

Moreover, the importance of the precedent set by the Federal Court of Appeal in *BP Canada* and the breadth of some of the statements made in that decision are also evidenced in the *Cameco* case. It is now clear that the courts are willing to go beyond a literal reading of the text of subsection 231.1(1) to ensure that reasonable and appropriate limitations exist on the powers of tax authorities to obtain taxpayer information. Even outside of the narrow confines of tax accrual working papers dealt with in *BP Canada*, courts faced with the task of interpreting the CRA's information-gathering powers will be quick to cite the statements of Chief Justice Marc Noël from that case to the effect that such powers are broad but not unlimited, must be interpreted in a larger context of working harmoniously with other laws to achieve results that Parliament would have intended, and cannot be used to compel taxpayers to reveal their soft spots.

Indeed, these cases show the difference between merely *reading* a provision and *interpreting* it. Statutory interpretation is an exercise in judgment based on legal principles developed over many years of jurisprudence (and are still developing). The role of the courts is to provide that judgment when tax authorities seek to push the boundaries of their powers beyond what is fair. One would expect to see more litigation in this area as the limits of what is permissible for tax authorities to do in the exercise of their audit function become more clearly defined and applied to particular cases. ■